BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION

In the Matter of	:	
Appropriate Framework for Broadband	:	**CC Docket No. 02-33**
Access to the Internet over Wireline Facilities	:	
	:	
Universal Service Obligations of Broadband	:	**CC Docket No. 95-20, 98-10**
Providers	:	

REPLY COMMENTS OF THE PENNSYLVANIA OFFICE OF CONSUMER ADVOCATE, THE MAINE PUBLIC ADVOCATE, THE MARYLAND OFFICE OF PEOPLE'S COUNSEL, THE OHIO CONSUMERS' COUNSEL, THE UTILITY REFORM NETWORK, THE CALIFORNIA OFFICE OF RATEPAYER ADVOCATES, THE CONNECTICUT OFFICE OF CONSUMER COUNSEL AND THE NEW HAMPSHIRE OFFICE OF CONSUMER ADVOCATE

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July 1, 2002

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LIST OF ACRONYMS

ADSL	Asymmetric Digital Subscriber Line
ARMIS	Automated Reporting Management Information System
ATM	Asynchronous Transfer Mode
BISP	Broadband Internet Service Provider
CA ORA	California Office of Ratepayer Advocates
CT OCC	Connecticut Office of Consumer Counsel
CLEC	Competitive Local Exchange Carrier
DLEC	Data Local Exchange Carrier
DSL	Digital Subscriber Line
DSLAM	Digital Subscriber Line Service Access Multiplexer
FCC	Federal Communications Commission
HUNE	High-Frequency Unbundled Network Element
ILEC	Incumbent Local Exchange Carrier
ISDN	Integrated Services Digital Network
ISP	Internet Service Provider
IXC	Interexchange Carrier
LEC	Local Exchange Carrier
LRIC	Long Run Incremental Cost
MBPS	Megabytes per Second
MD OPC	Maryland Office of the People's Counsel
ME PA	Maine Public Advocate
NASUCA	National Association of State Utility Consumer Advocates
NH OCA	New Hampshire Office of Consumer Advocate
NPRM	Notice of Proposed Rule Making
NYSDPS	New York State Department of Public Service
OFTEL	Office of Telecommunications (United Kingdom)
OH OCC	Ohio Consumers' Counsel
PA OCA	Pennsylvania Office of Consumer Advocate
PA PUC	Pennsylvania Public Utility Commission
PICC	Primary Interexchange Carrier Charge
PSTN	Public Switched Telephone Network
SBC	SBC Communications, Inc.
SLC	Subscriber Line Charge
SNET	Southern New England Telephone Company
TELRIC	Total Element Long-Run Incremental Cost
TFP	Total Factor Productivity

TSLRIC	Total Service Long-Run Incremental Cost
UNE	Unbundled Network Element
TURN	The Utility Reform Network
UNE	Unbundled Network Element
USF	Universal Service Fund
VDT	Video Dialtone
xDSL	Digital Services Line (Symmetric or Asymmetric)

1 INTRODUCTION

On February 15, 2002, the Federal Communications Commission ("FCC") released a Notice of Proposed Rulemaking ("NPRM") in the above-captioned proceeding launching an examination of the appropriate legal and policy framework under the Telecommunications Act of 1996 ("TA-96") for broadband access to the Internet provided over domestic wireline facilities. Comments were submitted by the State Consumer Advocates on May 3, 2002, and this submission constitutes our Reply Comments.

The Pennsylvania Office of Consumer Advocate ("PA OCA"), the Maine Public Advocate ("ME PA"), the Maryland Office of People's Counsel ("MD OPC"), the Ohio Consumers' Counsel ("OH OCC"), the California Office of Ratepayer Advocates ("CA ORA"), New Hampshire Office of Consumer Advocate ("NH OCA"), and the Connecticut Office of Consumer Counsel ("CT OCC") are each individually authorized by their respective state statute to represent the interests of utility consumers in their state in both state and federal courts and agencies.[1] The Utility Reform Network ("TURN") is a non-profit consumer advocacy organization that has represented the interests of California residential and small business telecommunications ratepayers before state and federal regulators since 1973 and joins in these Comments as well. The PA OCA, ME PA, MD OPC, OH OCC, CA ORA, CT OCC, NH OCA, and TURN (collectively referred to as "State Consumer Advocates") are actively involved in

1. See 71 P.S. §309-2 (PA OCA); 35-A MRSA section 1700 et seq. (ME PA); Md. Ann., PUC Sec. 2-201 – 2-205 (1999) (MD OPC); Chapter 4911, Ohio Rev. Code (OH OCC); State of California Public Utilities Code Section 309.5(a)-(g) (CA ORA); Connecticut General Statutes §16-2a (CT OCC); New Hampshire RSA 363:28 (NH OCA).

representing consumer interests in telecommunications issues and are, therefore, familiar with the issues contained in this NPRM.[2]

2 SUMMARY OF COMMENTS

The State Consumer Advocates see no need to reiterate all of the finding and recommendations submitted in the original Comments for this proceeding. These Reply Comments emphasize the following findings and recommendations:

Classification Of Wireline Broadband Internet Access Services

- Reclassifying Wireline Broadband Internet Access Service Providers As "Information Services" Is A Fundamental Error; Rather, The FCC Must Continue To Recognize That Much Of Wireline Broadband Internet Access Service Remains A Telecommunications Service (Section 3.1.1); and

- Reclassifying Wireline Broadband Internet Access Services As "Information Services" May Slow The Deployment Of Advanced Telecommunications Capability Under Section 706 Of TA-96 (Section 3.1.2).

Cost Allocation Issues

- The ILECs' Request For A Level Playing Field Only Goes So Far -- They Want A Tilted Field That Subsidizes Their Offerings Of Advanced Telecommunications Services (Section 3.2.1);

- The Consumer Advocates' Approach To Cost Allocation Parallels A Previous Decision Of The Commission With Regard To Cable Television, And This Suggests That The Proposed Methodology Is Consistent With The Commission's Overarching Policy And Objectives (Section 3.2.2);

- Price Caps Do Not Make Cost Allocation Irrelevant, As Has Been Recognized By The

2. Gabel Communications of Massachusetts assisted with the production of this document, particularly with regard to the cost allocation issues.

Commission And Congress (Section 3.2.3);

- If The Commission Deregulates Advanced Telecommunications Services, And Fails To Allocate Costs To These Services, The Price Cap Procedure Will Provide An Implicit Subsidy To Advanced Telecommunications Services (Section 3.2.4); and

- Cost Allocation Rules Cannot Be Put Aside By The Application Of Section 706 (Section 3.2.5).

Universal Service Issues

- Requiring All Broadband Service Providers To Contribute To Universal Service Support Is The Most Effective Means For The FCC to Preserve And Advance The Universal Service Support Mechanism (Section 3.3.1).

3 COMMENTS

3.1 Classification Of Wireline Broadband Internet Access Services

3.1.1 Reclassifying Wireline Broadband Internet Access Service Providers As "Information Services" Is A Fundamental Error; Rather, The FCC Must Continue To Recognize That Much Of Wireline Broadband Internet Access Service Remains A Telecommunications Service

The State Consumer Advocates submit that wireline broadband Internet access services should not be reclassified as "information services." Furthermore, arguments that support this reclassification are without merit and should be rejected. For example, SBC Communications, Inc. and Verizon support this reclassification but their arguments lack merit. Both SBC and Verizon assert that wireline broadband Internet access service should be regulated only under Title I.[3] SBC does so by saying that there is a single service, which is an information service.[4]

3. SBC Comments at 4; Verizon Comments at 1.

Verizon does this by saying that the broadband service component of wireline broadband Internet access is a standalone service, which is an information service.[5] These theories cannot both be right.

SBC overlooks the way in which telecommunications services are bundled together. When local and long distance service are bundled together, that does not make the bundle a single service. Nor is a single bundled service made when basic service and vertical services are bundled together. Neither can bundling wireline broadband service with Internet access service make the bundle a single service.

SBC's argument that wireline broadband Internet access is a single service depends entirely on the Commission's holding that cable modem Internet access is a single service.[6] SBC's -- and the Commission's -- fundamental error is in failing to recognize that a consumer can have a choice of ISPs whether the broadband service is provided over cable or over the LEC's wireline. Thus there are two services involved that may -- or may not -- be bundled together. The fact that often the two services are supplied by the same carrier, or by affiliates, does not transform the

4. SBC Comments at 16.

5. Verizon Comments at 9. Verizon also says that "bundled" broadband Internet access is an information service. Id. at 7. As with SBC, a bundled service cannot be transformed into a single service. The remainder of Verizon's argument focuses on the broadband transmission component of the bundle.

6. SBC Comments at 16.

two services into a single service. Equally, the fact that some providers of wireline broadband service do not give their customers a choice of Internet service providers to use with the broadband service does not transform the two services into a single service.[7]

In its Comments, Verizon argues that broadband transmission is "telecommunications," not a "telecommunications service."[8] But Verizon's argument consists of discussing how the Commission has treated other services, and that the Commission should not regulate broadband transmission.[9] Yet, Verizon never directly addresses why broadband transmission is not a telecommunications service.[10] In effect, Verizon frames the argument as whether the Commission should affirmatively regulate broadband transmission. Given the current state of the law, the question is actually whether the Commission should deregulate broadband transmission. Neither Verizon nor SBC provides any compelling reason why that should be so.

7. The recent decision of the D.C. Circuit Court of Appeals in USTA v. FCC, No. 00-1012 (May 24, 2002) reversing the Commission's line sharing order may reduce consumers' already limited choices in this regard.

8. Verizon Comments at 9.

9. Verizon Comments at 10-15; see also SBC Comments at 2.

10. Verizon Comments at 12.

Furthermore, SBC and Verizon argue that the Commission is required to regulate wireline broadband transmission in the same fashion as it has chosen to deregulate cable modem Internet access.[11] From the State Consumer Advocates' perspective, it would be compounding the error to base an unreasonable decision for ILECs on an unreasonable decision for cable companies. SBC's and Verizon's argument misses the fundamental point that regardless of how cable modem broadband service and the bundled ISP service are regulated, wireline broadband service remains a telecommunications service and must be regulated as such.

Verizon characterizes the Commission's current regulation of broadband transmission as based on only an assumption, as the product of "regulatory creep," and as the result of mere reflex.[12] Verizon also argues that regulating broadband transmission as a Title II service raises "serious First amendment concerns…."[13] However, this argument fails because the same could be said, of course, of Title II regulation of any service, which has never been globally challenged on First Amendment grounds.

11. SBC Comments at 4; Verizon Comments at 23-30.

12. Verizon Comments at 11.

13. Verizon Comments at 27-30.

Verizon also argues ways in which imposing unbundling requirements on broadband transmission may increase the costs of the service.[14] Here again, Verizon and SBC fail to ground this theory in reality by giving an indication of the amount of the increased cost, so that the cost can be compared to the competitive benefit.[15] As SBC describes them, the costs are the same sort of costs that accompany the transition from any monopoly market with bottleneck facilities to a competitive market that utilizes those facilities. If the LECs are not required to incur those costs, consumers will be doomed to service from a single ISP selected by (or affiliated with) their LEC.

SBC and Verizon describe, in detail, the impact that replacement of Title II regulation by Title I regulation will have on the market for wireline broadband transport.[16] The description shows that the impact will be devastating:

> *a.* The ILECs would no longer have to follow the 47 U.S.C. § 251 obligations, including unbundling and collocation.[17] Hence other

14. Verizon Comments at 20; see also SBC Comments at 15, 24-26.

15. Verizon also asserts that Title II regulation somehow prevents carriers from adopting "innovative pricing schemes" like those used by cable modem providers, Verizon Comments at 21, but does not identify any aspect of Title II regulation that has prevented *Verizon* from using such schemes.

16. SBC Comments at 4-6; Verizon Comments at 30-39.

carriers and ISPs unaffiliated with the ILEC could interconnect with ILEC and have access to the ILEC's bottleneck facilities solely on terms that the ILEC is willing to provide.[18]

b. The ILEC would be relieved of any obligations under the Commission's Computer Inquiries Orders.[19]

c. In its arguments, SBC first extensively discusses the Computer Inquiries Orders, and then dismisses the §251 requirements in less than a page.[20] The Act's requirement cannot be so easily evaded.[21]

17. SBC Comments at 4-5, 7, 31-32; Verizon Comments at 32. SBC would have the Commission "make clear that a wireline provider is not required artificially to structure any of its broadband information services to create a separate telecommunications service offering." SBC Comments at 6. "Artificial" here must be read as "against the ILEC's will."

18. See SBC Comments at 5. SBC states that "[b]ecause fewer than one-third of all broadband Internet access is provided over wireline facilities, requirements that LECs -- but not cable modem providers offer -- [ISPs] access serve little purpose." Id. at 14. The customers who have the choice of ISPs over wireline broadband facilities would not agree that this choice serves little purpose. SBC's position would restrict customer choice, and should be rejected for that very reason.

19. See Verizon Comments at 34-36.

20. SBC Comments at 18-32. It is not clear how germane the *Computer Inquiries* orders are to the current post-Act environment. This is why SBC's emphasis on the *Computer Inquiries* orders -- treating §251 as secondary, Id. at 31-32, -- shows the weakness of SBC's argument.

21. Section 251 applies to telecommunications services provided by LECs; there is no such requirement that applies to cable providers.

Neither SBC nor Verizon provide any basis for the Commission to conclude that deregulating wireline broadband transmission will actually result in more rapid deployment of broadband services.[22]

Both SBC and Verizon argue that the Commission must preempt state and local obligations.[23] SBC says that "the Commission must ensure that ILEC investment incentives are not undermined by a patchwork of inconsistent state regulation" and also discusses some parts of that "patchwork" that have impacted SBC.[24] Yet the discussion of the state actions in Ohio, Connecticut, Indiana, Wisconsin and California show that the actions were pro-competitive.

Verizon also complains about problems arising from regulating the telephone companies' retail rates for broadband transport. The State Consumer Advocates are unaware of any such regulation on the state or federal level. State efforts have been limited to regulating the telephone companies' wholesale rates for this service, and in requiring that the service be offered at wholesale in the first place.[25] States have also necessarily become involved in protecting

22. See SBC Comments at 2; Verizon Comments at 1.

23. See Verizon Comments at 39; SBC Comments at 32.

24. SBC Comments at 7, 33-34.

25. See, e.g., In the Matter of the Investigation Into Ameritech Ohio's InterLATA Service Under Section 271 of the Telecommunications Act of 1996, Case No. 00-942-TP-COI, Entry on

consumers from the sales and marketing tactics used by the ILECs for wireline broadband Internet access services.[26]

As such, reclassifying wireline broadband Internet access service providers as "information services" is a fundamental error and arguments to the contrary should be rejected. Rather, the FCC must continue to recognize that much of a wireline broadband Internet access services remain a telecommunications service so as to continue to support the goals and objectives of both Congress and the FCC articulated in, and arising from, TA-96.

Rehearing (date) at 8; Indiana Bell Telephone Company v. Indiana Utility Regulatory Commission, IURC Case No. 93A02-0107-EX-491, slip op. (March 12, 2002); Iglou Internet Services, Inc. v. BellSouth Telecommunications, Inc., Kentucky P.S.C. Case No. 99-484, Order (January 11, 2001); Petition of DSLNet Communications LLC Regarding Obligations of the Southern New England Telephone Company, Conn DPUC Docket No. 01-01-17, Decision (March 28, 2002).

26. California ISP Association, Inc. v. Pacific Bell Telephone Company, et al., CPSC Case 01-07-027, Assigned Commissioner's and Administrative Law Judge's Ruling Denying Defendant's Motion to Dismiss (March 28, 2002) at 10-12. In addition to the *California ISP Association* complaint, the CPUC has opened an investigation into the billing practices of Pac Bell, SBC ASI and Pacific Bell Internet Services with regard to DSL. CPUC Docket I.02-01-024, Order Initiating Investigation (January 23, 2002). This investigation has been consolidated with a complaint filed by The Utility Consumers' Action Network ("UCAN") against Pacific Bell, alleging cramming and unlawful delays in resolving cramming situations when brought to the Company's attention. See Order in Case 02-01-007 and I.02-01-024 (February 8, 2002).

3.1.2 Reclassifying Wireline Broadband Internet Access Services As "Information Services" May Slow The Deployment Of Advanced Telecommunications Capability Under Section 706 Of TA-96

In the NPRM, the FCC seeks comment on whether wireline broadband Internet access services should be classified as an "advanced telecommunications capability" and on what relevance, if any, that section 706 of TA-96 has to the issues raised in this proceeding.[27] Reclassifying wireline broadband Internet access services as "information services" may slow the deployment of advanced telecommunications capability under section 706 because the FCC and state commissions will have less regulatory authority over the retail and wholesale provision of such services.[28]

Section 706 specifically provides that "the Commission and each State commission with regulatory jurisdiction over telecommunications services shall encourage the deployment on a reasonable and timely basis of advanced telecommunications capability to all Americans."[29] This section further defines "advanced telecommunications capability" as "high-speed, switched,

27. NPRM at ¶29.

28. Consumer Advocates Comments at 26-27.

29. 47 U.S.C. §706(a).

broadband telecommunications capability that enables users to originate and receive high-quality voice, data, graphics, and video telecommunications using any technology."[30]

In their Comments, however, both SBC and Verizon misconstrue the broadband deployment mandates of section 706 of the Act and underestimate the impact on that mandate of reclassifying wireline broadband Internet access services as "information services." SBC and Verizon emphasize in their comments a notion of "intermodal competition at all costs," meaning that wireline broadband Internet access services should be given the same regulatory treatment as other forms of broadband Internet access services (*i.e.*, cable modems) seemingly without regard to what effect such treatment may have on other goals and objectives of both Congress and the Commission. However, as the State Consumer Advocates articulated in their Comments, Congress clearly intended to treat the telephone and cable industries differently when TA-96 was enacted and attempts by the FCC to treat these communication modes alike would effectively be rewriting TA-96.[31]

30. 47 U.S.C. §706(c)(1).

31. Consumer Advocates Comments at 9-11. The State Consumer Advocates submit that TA-96 is premised on the fact that, for many consumers, the last mile in the telecommunications network is and will remain a monopoly for a controlled bottleneck facility. Focusing on services delivered over that bottleneck, instead of on the existence of the bottleneck itself, misses the point. Congress intended consumers to have a choice of companies selling services over the telephone wires, not just a choice between a cable monopolist and a telephone monopolist.

The "mandate" of § 706(a) is merely to encourage broadband deployment, not to restructure the industry in a fashion, as discussed below, that will not encourage deployment. By contrast to § 706(a), § 706(b) is somewhat more forceful:

> The Commission shall, within 30 months after the date of enactment of this Act, and regularly thereafter, initiate a notice of inquiry concerning the availability of advanced telecommunication capability to all Americans … and shall complete the inquiry within 180 days after its initiation. In the inquiry, the Commission shall determine whether advanced telecommunications capability is being deployed to all Americans in a reasonable and timely fashion. *If the Commission's determination is negative, it shall take immediate action to accelerate deployment of such capability by removing barriers to infrastructure investment and by promoting competition in the telecommunications market*. [32]

Yet all three of the Commission's reviews to date have found that advanced telecommunications capability is being deployed in a reasonable and timely fashion.[33]

Importantly, the provision in § 706(a) that the Commission promote competition and encourage deployment of broadband services does *not* direct the Commission to preempt state

32. 47 U.S.C. § 706(b) (emphasis added). For purposes of this discussion, the difference between deployment of advanced telecommunications *services* in § 706(a) and advanced telecommunications capability in § 706(b) is not important.

33. In the Matter of Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, CC Docket No. 98-146, Third Report (February 16, 2002) at ¶1; Id., Second Report, 15 FCC Rcd 20913 (2000) at ¶ 1; Id., First Report, 14 FCC Rcd 2398 (1999) at ¶6.

action. This is especially true when it is the state actions that promote competition and deployment, contrary to SBC's view.[34]

In its Comments, SBC relies on the text of section 706 for the proposition that it is "the Commission's duty to 'remove barriers to infrastructure investment' for *all* broadband technologies" and that it would be "inconsistent with the Act to advance some technologies at the expense of others."[35] SBC cites Congressional testimony to show that "Congress understood that the Commission's duty was to harmonize regulation of different facilities-based broadband offerings that compete against each other."[36] This legislative history does *not* show that Congress intended the "harmonization" to reduce the amount of competition for the services, which is what would happen if the Commission treats wireline broadband services like cable broadband services.

34. SBC Comments at 35. In a recent decision of the Public Utilities Commission of Ohio, Ameritech Ohio (an SBC affiliate) was ordered to deploy advanced telecommunications services to Appalachian counties in southeastern Ohio as a remedy for the company's inadequate service. See also, In the Matter of Commission-Ordered Investigation of Ameritech Ohio Relative to its Compliance with Certain Provisions of the Minimum Telephone Service Standards, PUCO Case No. 99-938-TP-COI, Entry on Rehearing (June 20, 2002) at 38.

35. SBC Comments at 11; see also, Verizon Comments at 24.

36. SBC Comments at 12.

SBC also argues that "the Commission has an affirmative legal obligation to adopt a functional broadband approach that treats like services alike."[37] The State Consumer Advocates submit, however, that SBC's argument gives section 706 more authority than is allowed through a plain reading of all of TA-96. SBC is incorrectly extrapolating that section 706 would trump the specific provisions of the rest of TA-96 as well as efforts to promote broadband deployment by state commissions.[38]

For example, Congress specifically articulated many requirements for telephone companies in a separate section of TA-96 that are not to be applied to cable companies (*i.e.*, various interconnection requirements, negotiation and arbitration provisions, removal of barriers to entry, universal service, access by persons with disabilities, slamming and others). Had Congress sought to encourage "intermodal competition at all costs" as SBC and Verizon appear to argue, TA-96 would have not distinguished telephone service so much from cable service in the provisions of TA-96 which pertain specifically to telephone regulation.

37. SBC Comments at 12
38. See, footnote 61, infra.

SBC overstates TA-96's ability to preempt state action under section 706, especially where that state action also serves to promote broadband deployment. For example, SBC states in its comments that:

> in section 706 of TA-96, Congress directly instructed the Commission to use its regulatory jurisdiction to promote competition and to encourage deployment of broadband facilities. Inconsistent and intrusive state regulation undermines each of these statutory goals. [39]

This interpretation of TA-96 is incomplete because it fails to recognize those state actions which promote broadband deployment. Similarly, SBC also understates the effect that not declaring wireline broadband Internet access services as "information services" will have on unbundling requirements under section 251.[40]

SBC and Verizon further fail to recognize that reclassifying wireline broadband Internet access services as "information services" would actually limit competitive forces brought by CLECs who seek to provide competing broadband services. In supporting reclassifying wireline broadband Internet access services as "information services," Verizon and SBC argue that such a classification will increase intermodal competition but do not recognize that this reclassification will, in fact, reduce competition for the provision of broadband services within the

39. SBC Comments at 35.

40. SBC Comments at 25-27.

telecommunications industry. It is abundantly clear that Congress did not intend to sacrifice competition for the provision of broadband service between LECs in exchange for intermodal competition which SBC and Verizon tout as a panacea for broadband deployment.

Throughout their Comments, however, neither SBC nor Verizon provide any reason for the Commission to conclude that classifying wireline broadband Internet access services as "information services" will result in a more rapid deployment of broadband services. Verizon argues that it is the Commission's mandate under section 706 to "remov[e] barriers to infrastructure investment and promot[e] competition."[41] Verizon argues that regulating broadband transmission provides disincentives to carriers against providing the service.[42] Yet these theoretical generalities lack any clear support. Neither SBC nor Verizon identifies a single instance where the existence of Title II regulation has caused *SBC or Verizon* not to, for example, invest in the facilities needed to provide the service.[43]

41. Verizon Comments at 24.

42 See, e.g., Verizon Comments at 18, 20; see also SBC Comments at 13.

43. Verizon also cites to Kahn and Tardiff's affidavit for the proposition that Title II regulation will "result in less efficient firms supplanting more efficient ones." Verizon Comments at 18. Given Verizon's nationwide reach, and the fact that broadband transmission is currently regulated as a Title II service, it is curious that Verizon is unable to cite a specific example of this phenomenon.

However, the United States Supreme Court has recently acknowledged that CLECs have invested approximately $55 billion in broadband deployment since the passage of TA-96.[44] This tends to support that the competition between LECs under TA-96 is effective incentive and motivation for broadband infrastructure investment. The exclusively intermodal competition that SBC and Verizon propose is not in the public interest in light of the severe repercussions that may come from reclassifying wireline broadband Internet access services as "information services" such as failing to meet the other goals and objectives of Congress in passing TA-96.

As such, reclassifying wireline broadband Internet access services as "information services" may slow the deployment of advanced telecommunications capability under section 706 because the FCC and state commissions will have less regulatory authority over the retail and wholesale provision of such services. Therefore, the State Consumer Advocates submit that wireline broadband Internet access services should not be declared an "information service."

44. Verizon Communications, Inc. v. FCC, 535 U.S. __ (2002), slip op. at 46.

3.2 Cost Allocation Issues

3.2.1 The ILECs' Request For A Level Playing Field Only Goes So Far -- They Want A Tilted Field That Subsidizes Their Offerings Of Advanced Telecommunications Services

The ILECs repeatedly make level playing field type arguments vis-à-vis the cable companies. Nevertheless, they do not propose to allocate any costs to the advanced telecommunications services that are a primary driver of their costs.[45]

The need for a level playing field is exactly the reason that the State Consumer Advocates submitted their cost allocation proposal. The proposal guarantees that neither the ILEC nor the cable company is treated unfairly. The proposed allocation scheme would:

- not prevent ILECs from competing with their lowest priced rival, and
- provide an incentive, in the form of a shadow price on the shared telecommunications input, which would discourage anti-competitive pricing in broadband transmission (by ILECs subsidizing broadband entry from regulated services).

3.2.2 The Consumer Advocates' Approach To Cost Allocation Parallels A Previous Decision Of The Commission With Regard To Cable Television, And This Suggests That The Proposed Methodology Is Consistent With The Commission's Overarching Policy And Objectives

The ILECs argue that no cost allocation mechanism should be imposed on their operations in order to maintain parity between cable and telecommunications companies.[46] Contrary to the ILECs' arguments, the Commission has a long history of implementing a form of cost allocations in the cable industry where a supplier or buyer has market power. The FCC has implemented a pricing scheme for cable television that is not unlike what the State Consumer Advocates have proposed. In 1997 the Commission addressed the question of what price a cable television broadcaster should charge a content provider for inclusion of a channel at a particular retail tier or bundle of channels. The FCC's rule for à la carte (pay-per-view) channels is to charge the maximum implicit price paid for such channels.[47] The maximum implicit price for transmission of à la carte channels is simply the maximum per subscriber retail price for such channels less the programming fee the cable broadcaster pays the content provider.

This approach is very similar to that of the State Consumer Advocates. The State Consumer Advocates recommend allocating costs in a manner consistent with setting broadband

45. BellSouth Comments, *passim*; Comments of Fred Williamson and Associates, Inc., at 23-24; SBC Comments, *passim*; and Verizon Comments at 46.

46. See, e.g., BellSouth Comments at 26-27.

47. Federal Communications Commission, In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Leased Commercial Access, "Second Report and Order and Second Order on Reconsideration of the First Report and Order," CS Docket No. 96-60, Adopted: January 31, 1997; Released: February, 1997, FCC 97-27, at paragraphs 50-52; paragraph 13 provides a definition.

transmission prices equal to the minimum price charged by rivals, and where this is unavailable, to the price implied by the minimum retail price set by downstream rivals.[48] The only difference between the implied cost-covering price under the State Consumer Advocates' approach and the implied price for channel transmission is that the *maximum* price as *set by the regulated firm* is used by the FCC, rather than the minimum price as set by the regulated firm's competition.

The FCC's rule for channels carried in bundled retail offerings, called tiers, is a variation on this that relies on the average price. This reflects the difference between pricing à la carte and pricing an element of a bundle. The tier rule, however, remains similar to that proposed by the State Consumer Advocates:

> "[I]f subscribers pay an average of $0.50 per channel for a particular tier, and the average programming or license fee on the tier is $0.10, then, on average, programmers on the tier are implicitly "paying" the operator $0.40 for carriage."[49]

For present purposes, the use of the (actual or implied) minimum price of the ILEC's independent rivals makes more sense than using the ILEC's broadband transmission prices (actual or implied). If the ILEC's own prices were used it would be tempted to subsidize entry

48. The cost allocation is set equal to the actual or implied broadband transmission price less the incremental costs of the service.

49. In the Matter of Implementation of Sections of the Cable Television Consumer Protection and Competition Act of 1992: Leased Commercial Access, CS Docket No. 96-60, Second Report and Order and Second Order on Reconsideration of First Report and Order (rel. Feb. 1997), at ¶¶50-52.

into broadband transmission. It could achieve this by cutting price substantially below market rates. This would allow the ILEC to gain market share in broadband transmission without losing any revenues earned on its shared infrastructure. A cut in price would simply generate a concomitant increase in the cost recovery from regulated services. The minimum of the independent suppliers' prices is obviously attractive as, given rivals' prices must be used, it most likely best reflects costs.

3.2.3 Price Caps Do Not Make Cost Allocation Irrelevant, As Has Been Recognized By The Commission And Congress

Some of the responses have argued that price caps make cost allocation irrelevant.[50] Even if this were true:

- A ruling is necessary where price caps are not in place in all jurisdictions and because they might be removed. The FCC cannot base its policy on the proposition that all interstate carriers and all states will always have price cap regulation. Clearly, not all interstate carriers are subject to price cap regulation; nor do states rely on price cap regulation today and neither will they tomorrow.

- TA-96 requires such an allocation and the FCC must meet its statutory obligations under section 254(k).

- The FCC should not leave this issue to the States to resolve, as suggested by Verizon.[51] The FCC has determined that information services are interstate products. It makes sense

50. BellSouth Comments at 33-34. BellSouth argues that price caps eviscerate the need to address the 254(k) issue; Comments of SBC in this Proceeding SBC also argues that price caps address the cross-subsidy issue. SBC Comments at 21-22.

51. Verizon Comments at 37.

for the FCC to allocate these costs. One way or the other, however, some regulatory body must perform a cost allocation. State Consumer Advocates note that Verizon appears to favor allowing the States to allocate costs, while BellSouth is against it.[52]

That price caps do not remove the need for a cost allocation has been recognized by the FCC (on more than one occasion),[53] Congress,[54] and other comments.[55]

3.2.4 If The Commission Deregulates Advanced Telecommunications Services, And Fails To Allocate Costs To These Services, The Price Cap Procedure Will Provide An Implicit Subsidy To Advanced Telecommunications Services

52. BellSouth Comments at 33-34.

53. In the Matter of Price Cap Performance Review for Local Exchange Carriers; Treatment of Video Dialtone Services Under Price Cap Regulation, CC Docket No. 94-1, Second Report And Order And Third Further Notice Of Proposed Rulemaking, FCC 95-394, Adopted: September 14, 1995, Released: September 21, 1995, at ¶4. In the Matter of Implementation of the Telecommunications Act of 1996: Accounting Safeguards Under the Telecommunications Act of 1996, CC Docket No. 96-150, Report and Order, FCC 96-490, Adopted: December 23, 1996, Released: December 24, 1996, at ¶271.

54. Our submission deals with these matters generally at Section 7.3. Congress must have thought price caps did not obviate the need for cost allocations as TA-96 was passed 4 years after price caps were implemented (on implementation see, for example, Comments of BellSouth in this Proceeding, p. 28).

55. Comments of State Members of Separations Boards in this Proceeding (at pp. 2-3) recognize the need to allocate costs to non-regulated operations of the holding company through part 64 process, as does TimeWarner, at pp. 22-23 (TimeWarner also argues any cost allocation process would be arbitrary, but the State Consumer Advocates' approach, being based on market prices, is not arbitrary in the way that the cost allocations generally are).

As an additional response to BellSouth and SBC, the Commission's price cap procedures do not provide protection to customers of services that are included in the definition of universal service. Price caps provide a mechanism to annually change a regulated firm's prices. The adjustment mechanism reflects the difference between the annual rate of change in the productivity of the telecommunications market relative to the rest of the economy.

A price-cap approach is designed to simulate a company's cost conditions and pricing responses as if the company were operating in a competitive, unregulated environment. A company making rapid technological progress will experience significant declines in the cost of its inputs per unit of output. The technology changes enable a more efficient use of the inputs, and thus the firm experiences a lower cost of production for a given product. In a competitive market, where other firms are also experiencing this increased productivity, the firm will respond to the lower cost by reducing its price for that product. A price-cap mechanism mimics the competitive situation by forcing the regulated industry price to reflect any productivity gains.

The following simple example illustrates this point:

Suppose that a firm can produce voice telephone and DSL service. Telephone service is the subject of a price cap regulation mechanism, while DSL service is unregulated. Let us first examine a hypothetical Total Factor Productivity (TFP) computation for a firm producing only telephone messages.

Table 1 -- Total Factor Productivity Computation For A Firm Producing Only Telephone Messages

	Growth Rate	Expense Share	Weighted Average
Capital	+1.0%	0.40	+0.4%
Labor	-3.0%	0.40	-1.2%
Materials	-1.0%	0.20	-0.2%
Total Input			-1.0%
Total Output			+6.0%
Total Factor Productivity		+7.0%	

The Total Factor Productivity is computed as the assumed total output growth rate, 6%, less total input growth rate, -1%, for services.[56]

If advanced telecommunications services are deregulated, DSL services will not appear in total output growth, because neither the Commission nor the ILECs include deregulated services in their output measurements. However, unless there is a means to separate capital, labor, and materials used to produce telephone messages versus those used to produce DSL services, the rest of the table will be different, as in the following example.

Table 2 -- Total Factor Productivity Computation For A Firm Producing Both Telephone Messages And DSL Service

	Growth Rate	Expense Share	Weighted Average
Capital	+2.0%	0.40	+0.8%
Labor	+1.0%	0.40	+0.4%
Materials	+1.0%	0.20	+0.2%

56. See Broadband NPRM ¶¶7, 12 (discussing reengineering of the network).

Total Input	+1.4%
_____	
Total Output	+6.0%
Total Factor Productivity	+4.6%

Once again, note that TFP growth equals total output growth less total input growth. In Table 2, we have TFP = 6.0% - 1.4% = 4.6%, which is 2.4 percentage points less than in Table 1.

Tables 1 and 2 illustrate the fact that, if a TFP study is conducted for a firm that produces both regulated and unregulated products, and if there is no separation of the inputs used for the two types of products, the TFP study for regulated services will significantly understate the amount of true productivity growth in the firm. Since the TFP of the firm is understated, regulated products will be offered at a supra-competitive level and thereby providing a subsidy to unregulated services. The subsidy occurs because the costs of the upgrades are effectively charged to the regulated services.

Further, the existing caps at both the State and Federal level do not account for any regulated broadband services, as they were not important when the caps were last set (1998-1999).[57] Therefore, current caps entirely fail to take account of developments in broadband and this will continue so long as the FCC continues to exclude unregulated services from the measurement of output. This will also distort estimates of TFP change. If broadband grows more quickly than the outputs currently included when the TFP estimates are made, then the measured TFP growth will underestimate actual TFP change.[58]

BellSouth also contends that:

> "With regard to the requirement that services included within the definition of universal services should bear no more than a fair share of joint and common costs, the requirement is a ratemaking question, which, for the most part, falls within the jurisdiction of the state commissions"

57. See, e.g., Further MPRM, FCC 99-345, November 15, 1999.

58. The implicit subsidy can not be easily rectified through a modification of the current price cap regime. A reform of the existing price caps would require monitoring of the outputs and inputs of the unregulated operations of the ILECs. Further, price rise or declines in unregulated services would have to be taken into account in considering whether the cap had been complied with. Both types of activity are contrary to the treatment of unregulated lines of business and indeed might lie outside of the FCC's jurisdiction.

This is patently incorrect. Twenty-five percent of the cost of the loop is allocated to the interstate jurisdiction and that cost is recovered through the interstate subscriber line charge.[59]

3.2.5 Cost Allocation Rules Cannot Be Put Aside By The Application Of Section 706

SBC argues that cost allocation rules can be ignored under the imperative of section 706,[60] which requires the promotion of advanced telecommunications services. However, this neither makes sense in economic or legal terms. It is not clear cost allocation rules in general stand in the way of promoting advanced telecommunications services, but in any case, the State Consumer Advocates' proposal establishes parity with alternative suppliers, that is, is designed to encourage economically efficient development of advanced services in the form of broadband. Indeed, the approach provides market-based incentives to this effect.

59. In the Matter of Cost Review Proceeding for Residential and Single-Line Business Subscriber Line Charge (SLC) Caps, CC Docket No. 96-262, Order (June 5, 2002) at ¶1, n. 4.

60. SBC Comments at 27.

Moreover, Congress's explicit direction on cost allocations cannot be generally overridden by the more general language of section 706 which contains no explicit repeal of section 254(k).[61]

3.3 Universal Service Issues

3.3.1 Requiring All Broadband Service Providers To Contribute To Universal Service Support Is The Most Effective Means For The FCC to Preserve And Advance The Universal Service Support Mechanism

The State Consumer Advocates, like SBC, submit that an expansive approach to universal service contribution requirements is in the public interest; that is, it is in the public interest for all providers of broadband services to contribute to universal service support.[62] Such broad-based support is also in accord with the principles announced in section 254 of TA-96.

61. See, Morton v. Mancari, 417 U.S. 535, 94 S.Ct. 2474, 41 L.Ed.2d 290 (1974)(where there is no clear intention otherwise, specific statute will not be controlled or nullified by a general one, regardless of priority of enactment); Morales v. TransWorld Airlines, 504 U.S. 374, 112 S.Ct. 2031, 119 L.Ed.2d 157 (1992)(it is a commonplace of statutory construction that the specific governs the general); United States v. Prescon Corp., 695 F.2d 1236, 1243 (10th Cir. 1983)(it is a familiar rule of statutory interpretation that a specific provision will govern notwithstanding the fact that a general provision, standing alone, may include the same subject matter).

62. State Consumer Advocates at 77; SBC Comments at 41-42.

Section 254(b)(2)of TA-96 directs the FCC to establish policies to make available, in all regions of the Nation, advanced telecommunications and information services. At the same time, section 254(b)(4) requires that universal service contributions be equitable and non-discriminatory. In addition, the State Consumer Advocates agree with SBC in that section 254(d) provides the FCC with the authority to collect universal service contributions from all ISPs. The universal service requirements advanced by the State Consumer Advocates and SBC have support in all provisions of the Act.

Requiring all providers of broadband access to contribute to universal service is the most reasonable method through which the FCC can preserve and advance universal service in an equitable and non-discriminatory manner in this context. The FCC should not place the funding of universal service support in peril by, in effect, reducing funding sources by regulating down to the level of the least-regulated technology platform. That policy would indeed be dangerous given the rapid and unpredictable advances in the platforms used to provision broadband service.

Rather, the FCC should seek to bring all competitors to the same level by requiring all those entities that provide broadband access to contribute to universal service support regardless of facilities ownership. In addition, the Congress could not have intended for the FCC to adopt a

method of "leveling the playing field" that in fact places the future of nation-wide universal service in peril; to exempt broadband service from any contribution would do just that.

For example, Verizon's approach of exempting all but school and library broadband services from universal service support would not preserve and advance universal service.[63] In fact, Verizon's crabbed approach to universal service requirements would limit the availability of advanced telecommunications and information services.[64] The State Consumer Advocates therefore submit that Verizon's recommendations run counter to the purpose and requirements of TA-96. Verizon bases its recommendations on flawed conclusions; Verizon assumes to know that the FCC will not require cable, satellite, or terrestrial wireless broadband service providers to contribute to universal service support. Based on that assumption, the underlying theme of Verizon's comments is that the FCC should deregulate to the level of the least-regulated competitor.

63. Verizon Comments at 42-43.

64. Verizon Comments at 42-43. The State Consumer Advocates submit that our position does not mean that we support or do not support using universal service funds for broadband deployment.

As an initial response to Verizon's proposed scheme, the State Consumer Advocates note that the FCC stated that *this* proceeding, and not the Cable Modem Proceeding, will be the one in which the FCC will determine if cable-modem based Internet access providers should be required to support universal service.[65] In the Cable Modem Proceeding, the FCC refrained from determining whether cable modem-based Internet access providers should be required to contribute to universal service, and instead deferred to this proceeding to resolve that issue.[66]

Based upon the false premise that the FCC has already decided to exempt non-wireline broadband service providers from universal service support obligations, Verizon constructs three arguments in support of its position. First, it states that, to the extent possible, universal service contribution requirements should not put carriers at a competitive disadvantage.[67] Second, Verizon points to that provision of the Act that states that every carrier contribute on an equitable and non-discriminatory basis.[68] Finally, Verizon makes several unsupported arguments

65. Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities, et al., Docket Nos. GN 00-185, CS 02-52, Declaratory Ruling And Notice Of Proposed Rulemaking, ¶110 ("Cable Modem Proceeding") (2002).

66. Id.

67. Verizon Comments at 43.

68. Id.

suggesting that Verizon may have a basis to challenge any outcome other than an all-or-nothing scheme.[69]

First, as Verizon itself points out, the FCC's definition of the public interest underlying universal service support states that, *to the extent possible*, universal service obligations should not put carriers at a competitive disadvantage.[70] That definition clearly states a preference for universal service support over the competitive disadvantages that carriers may face because of that support. In addition, if the FCC requires all providers of broadband services to contribute to universal service support, this objection is moot.

As to Verizon's point regarding equitable and non-discriminatory contribution requirements, that argument also is moot if the FCC determines that all broadband service providers must make universal service support contributions. Finally, the FCC's permissive authority provides a sound basis upon which to execute the requirements of the Act by requiring all broadband service providers to contribute to universal service support. In that manner, the FCC will avoid

69. Id.

70. Id.

all of Verizon's tenuous bases for challenging a universal service support obligation that does not achieve parity among all platforms.

4 CONCLUSION

WHEREFORE, the Pennsylvania Office of Consumer Advocate, the Maine Public Advocate, the Maryland Office of People's Counsel, the Ohio Consumers' Counsel, the California Office of Ratepayer Advocates, the Connecticut Office of Consumer Advocate, the New Hampshire Office of Consumer Advocate, and The Utility Reform Network respectfully request that the Federal Communications Commission consider these Reply Comments when analyzing the legal and policy framework of broadband access to the Internet provided over domestic wireline facilities. In particular, the State Consumer Advocates submits that the FCC should not reclassify wireline broadband Internet access services as "information services." However, if such a reclassification is made, then the FCC must, at a minimum, make a ruling on cost allocation as per section

254 (k) of TA-96. The State Consumer Advocates recommend this be done using the market-base approach outlined in our original comments.

Respectfully submitted,

_____

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July 1, 2002

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July 1, 2002

Office of the Secretary
Federal Communications Commission
9300 East Hampton Drive
Capitol Heights, MD 20743

Re: Appropriate Framework for Broadband Access to the Internet Over Wireline Facilities
CC Docket No. 02-33
Universal Service Obligations of Broadband Providers
CC Docket No. 95-20, 98-10

Dear Secretary:

Enclosed please find an original and four copies of State Consumer Advocate's Reply Comments in the above-referenced matter. Please also note that these Reply Comments have been filed with the Commission electronically.

Please indicate your receipt of this filing on the additional copy provided and return it to the undersigned in the enclosed self-addressed, postage prepaid, envelope. Thank you.

Sincerely yours,

Joel H. Cheskis
Assistant Consumer Advocate

Enclosure

BEFORE THE
FEDERAL COMMUNICATIONS COMMISSION

In the Matter of	:	
Appropriate Framework for Broadband	:	CC Docket No. 02-33
Access to the Internet over Wireline Facilities	:	
	:	
Universal Service Obligations of Broadband	:	CC Docket No. 95-20, 98-10
Providers	:	

I hereby certify that I have this day served a true copy of the foregoing document, State Consumer Advocate's Reply Comments, upon parties of record in this proceeding dated this 1st day of July, 2002.

Respectfully submitted,

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